

A community welfare corporation that purchases and sells unimproved land and engages in other business activities, the profits from which are distributed to members, is not exempt under section 501(c)(4) of the Code.

Advice has been requested whether the corporation described below qualifies for exemption from Federal income tax as a social welfare organization under section 501(c)(4) of the Internal Revenue Code of 1954.

The corporation was formed for the stated purpose of promoting the general welfare of the residents of a particular community. Membership in the corporation was available to those who owned property in a designated area. They paid an assessment based on the amount of property owned. Membership is transferable to successive purchasers of property owned by the original members.

The corporate bylaws provide that any profits of the corporation shall be apportioned pro rata among the members according to the assessment originally paid.

The corporation used the original assessments to purchase unimproved lots and some undeveloped land in the area. Over the years, the corporation sold on a sporadic basis some of the property and received substantial income from such sales. It derived additional income from the investment of the proceeds from the sales. The corporation improved and maintained nonresidential property and engaged in other activities for the benefit of all the residents of the area. On several occasions the corporation distributed profits to the members in accordance with its bylaws provisions.

Section 501(c)(4) of the Code provides for the exemption of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(1) of the Income Tax Regulations states that an organization may be exempt under section 501(c)(4) of the Code if it is not organized or operated for profit and it is operated exclusively for the promotion of social welfare.

The corporation is authorized to make, and in fact made, distributions of profits to its members. These distributions are equivalent to dividends based upon equity ownership and result in profit to the members. It is held that the corporation does not qualify for exemption from Federal income tax under section 501(c)(4) of the Code since the authority for making the distributions and the distributions themselves are incompatible with the requirements of the regulations that an organization must not be organized or operated for profit.